United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLANT

ORIGINAL

CA 76-7492

United States Court of Appeals
FOR THE SECOND CIRCUIT

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P/S

DR. DAVID SIROTA, FRANCES NAISON, IDA SIROTA and JOHN P. LYCETTE, JR.,

Plaintiffs,

against

ECONO-CAR INTERNATIONAL, INC., WESTINGHOUSE ELECTRIC CORPORATION, JAMES W. CROWLEY, BERRIEN H. BECKS, and BERRIEN H. BECKS, WILLIAM FRANK O'ROURKE, and FLORIDA BANK AND TRUST COMPANY AT DAYTONA BEACH, as EXECUTORS OF THE ESTATE OF GUY B. ODUM.

Defendants.

JAMES W. CROWLEY and BERRIEN H. BECKS,

Third-Party Plaintiffs,

against

POWELL, GOLDSTEIN FRAZER & MURPHY, a partnership.

Third-Party Defendant.

ABRAHAM & CO. INC.,

Claimant-Appellant

against

SPINGARN & CO., INC., and SATNICK-JAPHA, INC.,

Claimants-Appellees

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR APPELLANT

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UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

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JAMES W. CROWLEY and BERRIEN H. BECKS, Third-Party Plaintiffs, -against- POWELL, GOLDSTEIN FRAZER & MURPHY, a partnership Third-Party Defendant,	
ABRAHAM & CO. INC., Claimant-Appellant -against- SPINGARN & CO., INC., and SATNICK-JAPHA, INC., Claimants-Appellees	

BRIEF ON BEHALF OF
APPELLANT, ABRAHAM & CO. INC.

Preliminary Statement

The decision of the district court in this case was rendered by Judge Charles M. Metzner. His opinion has not

been reported.

ISSUE PRESENTED FOR REVIEW

Whether the District Court erred in holding that on November 2, 1971 Satnick-Japha, Inc. ("Satnick") and Spingarn & Co., Inc. ("Spingarn") had beneficial ownership, in the aggregate, of 606 Interim Certificates of Westinghouse Electric Corporation (later to become 1,212 Interim Certificates because of a two-for-one split), and, therefore, that Abraham & Co. Inc. ("Abraham") was not entitled to share in the settlement fund created in the above captioned class action. (A 96).

STATEMENT OF THE CASE

A. Nature of the Case and Prior Proceedings

This appeal arises out of a class action brought pursuant to Sections 10(b) and 14(a) of the Securities Exchange act of 1934 in connection with the 1970 merger of Americar, Inc. ("Americar") with Westcar, Inc. ("Westcar"), a subsidiary of Westinghouse Electric Corporation ("Westinghouse") (A 9).

In the merger, Americar's shareholders were issued common shares of Westinghouse. To secure Westinghouse against certain liabilities, 16 per cent of the Westinghouse shares to be received by each Americar shareholder were placed in escrow, and Interim Certificates ("Interim Certificates") representing these escrow shares were issued to Americar shareholders (A 10).

For nearly one year following the merger, the Interim Certificates were traded in the open market. On October 29, 1971, two days before the deadline for claims under the escrow, Westinghouse asserted claims against the escrow which exceeded the value of the escrow shares, thereby rendering the Interim Cerificates worthless (A 10). In the class action, the plaintiffs alleged that the proxy statement issued in connection with the merger was misleading in its treatment of the escrow (A 11).

A settlement of the class action was negotiated, and by an Order and Judgment, dated July 15, 1975 (A 44-49), the District Court ordered the class action to be settled in accordance with a Stipulation of Settlement, dated March 31, 1975 (A 28-36), which provided that a settlement fund, consisting of 37,728 shares (post split) of Westinghouse common stock and $135,000.00, be divided amongst the class of persons who owned Interim Certificates on November 2, 1971.

The class had originally been defined, by Order dated February 7, 1974, as those persons who owned Interim Certificates on October 29, 1971 (A 19-20). The rationale for the change in definition, as set forth by plaintiffs, was as follows:

> As part of this Settlement, the Court is being asked to expand the classes so as to include persons who acquired Interim Certificates through November 2, 1971. This requested extension is due to the fact that even though Westinghouse made its claim against the escrow on October 29, 1971, the news did not become

> completely disseminated until November 2. The release was issued in Chicago late in the day on Friday, October 29. On Monday, November 1, there was some trading of Interim Certificates in New York, apparently at prices which reflect a lack of knowledge of the Westinghouse claim. Since Westinghouse's claim exceeded the value of the escrow, the claim effectively rendered the Interim Certificates worthless. Since plaintiffs are suing for the value of the Interim Certificates (plus interest and/or dividends) based upon the alleged misleading nature of the proxy statement, persons who sold Interim Certificates prior to November 2, 1971, under the aegis of the alleged misleading proxy statement, received substantial value for the Certificates based upon the expectation that Westinghouse would not assert a claim against the escrow. Therefore, it is questionable whether persons who sold Interim Certificates prior to November 2, 1971 suffered any damages. In fact, they were beneficiaries of the alleged nondisclosures. However, persons who held Interim Certificates on November 2, 1971 by which date the Certificates had clearly been rendered worthless, suffered damages. Consequently, the Settlement provides that only persons who held Interim Certificates on November 2, 1971 may participate in the Settlement. (A 42-43)[1]

Abraham, a shareholder of Americar at the time of the Westcar merger, submitted a proof of claim with respect to 1212 Interim Certificates (606 pre-split) (A 91). Whitman & Ransom, Esqs., attorneys for Westinghouse, rejected Abraham's proof of claim. (A 94). The rejection was made on the grounds that Satnick and

1. Neither the Defendants' Memorandum in Support of the Settlement nor the District Court's Decision (A 50) contained any discussion of the change in class definition.

Spingarn had submitted claims based on the same 1212 Interim Certificates, that only one party could file a claim based on any given certificate, and that "from the information submitted to [Whitman & Ransom] it appeared that Spingarn and Satnick had purchased the subject certificates on or prior to November 2, 1971 although the settlement did not take place until sometime thereafter..."[2] (A 92-3). The matter was thereupon presented to the District Court. Judge Metzner, deciding on the papers without a hearing, held that Satnick and Spingarn were the beneficial owners of the Certificates on November 2, 1971, and therefore that Abraham was not entitled to share in the settlement fund.

B. The Facts

Abraham, a shareholder of Americar at the time of the Westcar's merger on October 30, 1970, received a number of Interim Certificates in the merger transaction. Subsequently, Abraham purchased additional Interim Certificates in the open market (A 55-56).

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2. After the exchange of briefs below, Whitman & Ransom wrote to the District Court stating that "Westinghouse and Econo-Car... have no position concerning the outcome of the dispute other than the request that under no circumstances should more than a total of 1212 interim certificates be approved in connection with this dispute." (A 93)

On November 1, 1971, Abraham authorized a brokerage firm, Brukenfeld, Mitchell & Co. ("Brukenfeld"), to sell 606 Interim Certificates on Abraham's behalf in the over-the-counter market. In telephone conversations, conducted at about 10:00 A.M. on November 1, 1971, Satnick and Spingarn (hereinafter sometimes referred to collectively as the "Cross Claimants") agreed to purchase from Brukenfeld 406 and 200 Interim Certificates, respectively at a price of $65 per Interim Certificate (A 57). Shortly thereafter that same morning, the Cross Claimants telephoned Brukenfeld disavowing and cancelling the transaction alleging that material misrepresentations had been made (A 85,82). On November 4, 1971, when Brukenfeld failed to receive confirmation notices from the Cross Claimants with respect to the transaction, Brukenfeld delivered NASD 101 Forms to each of them, pursuant to Section 9(c) of the NASD Uniform Practice Code (A 79-80). The 101 Form is a notice by a broker who has confirmed a transaction (the "confirming broker") to the broker on the other side of the transaction (the "contra-broker") that no confirmation of the transaction has been received from the contra-broker (A 79-80). On receipt, the contra-broker must either affirm or "DK" (state that he Doesn't Know) of the trade. The Cross Claimants DKed the November 1, 1971 transaction (A 81,82).

On November 8, 1971 Brukenfeld, through its attorneys, wrote to each of the Cross Claimants advising them of its intention to make delivery of the Interim Certificates on the scheduled settlement date (A 81-82).[3] On the settlement date, when Brukenfeld tendered delivery of the certificates, Satnick rejected delivery, submitting a signed NASD Rejection Form 801 marked DK (A 83). Spingarn rejected delivery by returning the Brukenfeld delivery bill marked "Don't Know" (A 84). Subsequently, Spingarn wrote to Brukenfeld, in response to the letter of November 8, confirming its position that on the basis of certain material misrepresentations and the failure to disclose certain material information, Spingarn believed that it was not obligated to accept delivery of the Interim Certificates or to make payment therefor. (A 85)

For fifteen months following the foregoing events, Abraham remained the holder and undisputed owner of the 606 Interim Certificates, which on the morning of November 1, 1971 had a market value of Thirty Nine Thousand Three Hundred Ninety ($39,390.00) Dollars, but

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3. On November 1, Satnick agreed to purchase 387 Interim Certificates that Brukenfeld was selling for its own account, in addition to the 406 Interim Certificates that Brukenfeld was selling for Abraham. Satnick submitted a DK as to that trade as well (A 83). For this reason the Fried Frank letter of November 8, (A 82) and the Satnick Rejection Form (A 83) refer to a total of 793 Interim Certificates.

were thereafter believed to be worthless. Believing the DK of the transaction had been unjustified, Abraham initiated arbitration proceedings against each of Satnick and Spingarn seeking damages equal to the November 1 contract price on each trade [4] (A 87). In the arbitration proceedings, Satnick and Spingarn maintained that Brukenfeld and Abraham were guilty of improper conduct, that the unconsummated November 1 transaction had been voided and that they were not responsible to Abraham in damages. For fifteen months while the arbitration was pending, Abraham continued to hold the Certificates while pursuing its claims against Satnick and Spingarn, who remained firm in their assertion that the unconsummated transaction had been voided. Then in February 1973, before the matter was submitted to a hearing, a meeting was held amongst the parties at which it was agreed to settle the dispute. (A 58)

The settlement was embodied in a Stipulation of Settlement, dated February 5, 1973, portions of which provided as follows:

> 1. Satnick-Japha, Inc. ("Satnick") shall pay to Abraham & Co., Inc. (corporate successor to Abraham & Co., a New York limited partnership) ("Abraham") the sum of Twelve Thousand Seven Hundred Thirty Nine Dollars and Eight Cents ($12,739.08) in full settlement of Abraham's claim in arbitration

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4. Abraham's damages were equal to the difference between the November 1 contract price ($39,390 in the aggregate) and the post announcement market value ($0).

against Satnick in the amount of Twenty Six Thousand Three Hundred Ninety ($26,.390.00) Dollars pending before the National Association of Securities Dealers, Inc. ("NASD").

2. Spingarn & Co., Inc. ("Spingarn") shall pay to Abraham the sum of Six Thousand Two Hundred Sixty Dollars and Ninety-Two Cents ($6,260.92) in full settlement of Abraham's claim in arbitration against Spingarn in the amount of Twelve Thousand Nine Hundred Forty ($12,940.00) Dollars pending before the NASD.

[Paragraphs 3, 4 and 5 specify the delivery of releases and payments to Wolf, Haldenstein to be held in escrow]

6. On or before Tuesday, February 6, 1973, Abraham will deliver to Wolf, Haldenstein in escrow, 1212 Westinghouse Electric Interim Certificates ("Certificates") owned by it (after a two-for-one split) and which are the subject of the claims agreed to be settled upon written entry of "the award". The Certificates delivered hereunder will be duly endorsed and 812 such Certificates may be released by Wolf, Haldenstein to Satnick and 400 Certificates to Spingarn upon written notice of "the award".(emphasis added)

7. In the event the panel of arbitrators of the NASD fails to approve the settlement hereby agreed to by the parties, all releases, Certificates and payments will be returned to the respective parties who deposited them in escrow with Wolf, Haldenstein.

8. In the event the panel of arbitrators disapprove the Settlement hereby agreed to by the parties, no party hereto or representative of such party may refer to or make use of this Stipulation, the terms hereof, or any part or all of the negotiations or discussions incident thereto as evidence in any proceeding before the NASD or elsewhere relating to the claims herein.

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11. It shall be understood that the releases to be exchanged by the parties shall not be construed as an admission of liability or wrongdoing on the

part of any of the parties in the pending arbitration proceeding or for any other purpose and that any award rendered by the arbitration panel based on this Stipulation shall be final and deemed a collateral estoppel and, if reduced to a judgment in a court of competent jurisdiction, res judicata. (A 65-68)

On February 5, 1973, Abraham delivered the releases and Certificates to Wolf, Haldenstein (A 69), and subsequently the arbitrators rendered a decision approving the Stipulation (A 72-74). The conditions precedent set forth in the Stipulation having been met on February 27, 1973, the Settlement became effective on that date.

At the meeting at which the settlement was agreed upon, there was no discussion of any amendment, ratification, or consummation of the November 1 agreement (A 61). Mr. Stuart Sirdell, who attended the Settlement discussions on behalf of Abraham, stated the following in his affidavit submitted to the District Court:

> Essentially, the parties agreed (subject to approval by the arbitrators) that in consideration of Abraham's release of its claims against Satnick and Spingarn for damages in the aggregate amount of $39,390, they would pay Abraham the aggregate sum of $19,000 and release Abraham of any claims arising out of the November 1971 transaction. In addition, Satnick and Spingarn requested that at the same time the Certificates be assigned to them, to which Abraham agreed. At no time during the negotiation of the Settlement did Satnick, Spingarn, or their counsel state any intention or desire that Abraham assign title to the Certificates retroactive to November 1, 1971. Similarly, at no time in the drafting of the Stipulation did they request the insertion of any such

> language in the Stipulation. Abraham, acting through its officers, was not asked nor did it intend to assign title to the Certificates retroactive to November 1971. Abraham's assignment was clearly and unambiguously made in February 1973 as of February 1973 (A 55, 61-62).

It was Abraham's and Brukenfeld's understanding, at the time the Settlement was negotiated, that the November 1971 agreement had been cancelled (A 90). Further, the words "owned by it" appearing in Section 6 of the Stipulation were understood by Abraham as an acknowledgement by both parties that as at February 5th, 1973, Abraham was the owner of the Certificates (A 61).

ARGUMENT

POINT I

Abraham suffered damages that the Class Action was designed to redress.

On the morning of November 1, 1971, Abraham owned Certificates having a then market value of $39,390., which later in the day were rendered worthless. Taking into account the $19,000 received by Abraham from Satnick and Spingarn in 1973, Abraham remains with a loss of $20,390.00 caused by the wrong the class action was brought to redress.

On the other hand, the Cross Claimants will have suffered no loss if Judge Metzner's decision is upheld, and indeed, based on the current value of Westinghouse

shares and the settlement fund, they will enjoy a slight profit.

Plaintiff's brief in support of the proposed Settlement makes it clear that the intent of the class definition was to allocate the settlement fund to those who sustained a loss on the Interim Certificates as a result of Westinghouse's assertion of a claim against the escrow. Abraham has an equitable claim to a portion of the settlement fund because it sustained such a loss.

In 1973, when Abraham and the Cross Claimants agreed that the loss of $39,390 should be divided roughly evenly between them, they all believed the Interim Certificates worthless, and were apparently unaware of the class action. Feeling that a similar division of the value of the Certificates would have been made in 1973, if the parties had then known of their potential value, Abraham considered an equitable division of the portion of the class action settlement fund allocable to the 1212 Interim Certificates to be appropriate. Because that offer was unacceptable to Satnick and Spingarn, Abraham here asserts its legal right to participate in the class action fund as the legal and beneficial owner of the 1212 Interim Certificates on November 2, 1971.

POINT II

Abraham remained owner of the Interim Certificates until February 1973.

Pursuant to Section 9(c)(3) of the NASD Uniform Practice Code, the DK of a transaction by a contra-broker relieves the confirming broker of any further duty or liability on the transaction. In the instant case, Satnick and Spingarn each submitted a DK of the transaction, and subsequently rejected delivery of the securities. Brukenfeld, the confirming broker, and Abraham, its principal were thus relieved of any liability arising out of the November 1 agreement to sell Interim Certificates.

Abraham, however, retained a claim against Satnick and Spingarn for the alleged wrongful cancellation of the November 1 trade, and Abraham pursued that claim in the NASD arbitration.

It appears that the District Court concluded, based upon a reading of Section 1(b) of the NASD Uniform Practice Code, that the November 1 agreement remained in force. From that premise - an erroneous one, as we shall demonstrate - Judge Metzner reasoned that Abraham's failure to resort to the remedies of Section 59 and 60 of the

Uniform Practice Code [5] manifested its intention to affirm the transaction, wherefore it must have considered the transaction a sale on Noveber 2. Section 1(b), however, deals with the failure deliver and the failure to pay for securities pursuant to confirmed contracts. That such is the fact is abundantly established by the references to Sections 59 and 60 as the remedy of the party not in default.

Section 59 gives the buyer under the unsettled contract the right to "buy-in" the securities which the seller failed to deliver, but the condition precedent to the buyer's right to "buy-in" the seller is the possession of the original comparison of the "broker/dealer to be 'bought-in', evidencing the contract to the closed out" i.e. the seller's confirmation of the transaction.

Section 60 gives the seller under the unsettled contract the right to "sell-out" the securities which the buyer failed to receive, but the condition precedent to the seller's right to "sell-out" the buyer is that the seller should not have received a rejection of the contract on Form 801.

It follows from the above that Section 1(b) does not apply to the instant situation in which there was a DK of the transaction followed by a rejection of delivery

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5. Section 59 is the "Buy-in" procedure available to the purchaser from a defaulting seller and thus could not have been available.

and the submission of a Rejection Form on Form 801 in accordance with Section 52 of the Uniform Practice Code. On the given facts, pursuant to Section 9(c)(3) of the Uniform Practice Code, Abraham and Brukenfeld were relieved of any duty or liability on the November 1 transaction.

In fact, Abraham was enforcing the only remedy available to it, namely to establish via arbitration that there was a conract between the parties, that the buyer under the contract had breached it and that Abraham was entitled to an award of damages on account of the breach. That the damages sought equaled the price was a fortuitous circumstance attributable to the then belief that the Interim Certificates were valueless. If the arbitrators had determined that the certificate had some value and had awarded Abraham less than the contract price, would Satnick and Spingarn contend that they were the owners of the Certificates? Obviously not.

As a result of the settlement of the dispute in 1973, the rights of the parties arising out of the events of early November 1971 were never judicially determined. By the terms of the Stipulation of Settlement, the parties agreed never to raise and are now collaterally estopped from raising the questions of whether Abraham was entitled to damages for the contract cancellation, or whether Satnick and Spingarn were

justified in their DK of the trade. Those questions are not before this court.

The question is who owned the certificates on November 2, 1971. Abraham respectfully submits that it owned the certificates on the morning of November 1, and by reason of the DK of the transaction and the rejection of delivery, it continued to own the certificates until it sold them to the Cross Claimants pursuant to the terms of the 1973 settlement agreement.

Under the law of the State of New York, the effect of the settlement was to substitute the mutual promises contained in the settlement agreement for all obligations contained in or arising out of the disputed agreement. Putnam v. Otsego Mutual Fire Insurance Company, 45 A.D.2d 556, 360 N.Y.S. 2d 331 (3rd Dept. 1974), Gaffey v. St. Paul F. & M. Insurance Co., 221 N.Y. 113, 120, 116 N.E. 778 (1917). When parties to a bona fide dispute enter into a contract settling their existing controversy, the settlement agreement supersedes and extinguishes the contract on which the original claim was based, unless a contrary intent is expressed. Moers v. Moers, 229 N.Y. 294, 300, 128 N.E. 202 (1920). In re Kellet Aircraft Corp., 173 F.2d 689, 692 (3rd Cir. 1949); see Durasteel Co. v. Great Lakes Steel Corp., 205 F.2d 438, 441-442, (8th Cir. 1953), Aktieselskabet Dampskibsselskabet S. v. U.S., 130 F. Supp. 363, 367 (Ct. Cl. 1955) (and cases therein cited).

All rights of the parties with respect to the Certificates are, therefore, to be determined by reference to the Stipulation, and the issue before this Court is what rights in the Certificates did Abraham contract to assign to Satnick and Spingarn in the Stipulation of Settlement.

The plain and clear meaning of the Stipulation and Settlement was that Abraham was to deliver the Interim Certificates to Wolf, Haldenstein in escrow, and that subject to the receipt by Wolf, Haldenstein of all of the other items required to be deposited with it, and the approval of the NASD arbitration panel, such delivery would constitute a transfer of ownership of the Certificates to Satnick and Spingarn. Janos v. Peck, 21 A.D.2d 529, 251 N.Y.S.2d 254 (1st Dept. 1964) aff'd, 15 N.Y. 2d 509, 202 N.E. 2d 560; UCC Section 8-313 (1)(a).

Nothing in the Stipulation of Settlement suggests any intention of the parties that anything other than current ownership of the shares was to be transferred, and at the time the settlement was negotiated there was no request that the assignment include anything other than current ownership.

It may well be that the parties gave no thought to the matter, believing that the Interim Certificates were worthless and would remain worthless. In such

case, the parties cannot be presumed to have had any intent other than to effect a transfer of ownership of the certificates as of the date of delivery.

From the opinion of the District Court, it appears that relying on Section 1(b) of the NASD Uniform Practice Code, Judge Metzner concluded that the November 1 trade was never cancelled, and on the basis of that holding, further concluded that from and after November 2, 1971, by reason of Abraham's prosecution of its arbitration claim, Satnick and Spingarn had beneficial ownership of the Interim Certificates, which fact was unaffected by the terms of the Settlement Agreement. We respectfully submit that this conclusion is incorrect, as a matter of law, for the following reasons:

1. As we have demonstrated, Section 9 of the Uniform Practice Code governs the instant facts and not Section 1(b).

2. The initiation of arbitration proceedings against Satnick and Spingarn did not affect an equitable assignment of Abraham's ownershp in the Interim Certificates. That argument, urged below, is based upon the estoppel concept that Judge Metzner correctly rejected as "of little use" in determining ownership.

3. In an attempt to distinguish the cases cited for the proposition that the settlement

agreement had the effect of extinguishing all liabilities under the disputed agreement, Judge Metzner suggests that Satnick and Spingarn are not attempting to enforce the term of the November 1 agreement that would have given them beneficial ownership on that date, but were simply attempting "to advert to a state of affairs that existed at a given date." As at any date prior to February, 1973, the Cross Claimants neither had nor claimed any ownership of the Certificates, and but for the Stipulation of Settlement, the Cross Claimants would not have had ownership of the Certificates, record or beneficial. Thus, such ownership as they now have must find its source in the Stipulation of Settlement. That document makes it clear that Abraham was the owner of the Interim Certificates on November 2 and at all times thereafter until the Settlement Stipulation became effective.

4. No support for the District Court holding is found in Tangorra v. Hagan Investing Corporation, 38 A.D.2d 671, 327 N.Y.S. 2d 131 (4th Dept. 1971), to which citation was made. That case, which involved a dispute between a broker and his own customer, stands for the proposition that when a broker purchases stock on behalf of his customer by exchanging written confirmations with the selling broker and sending a confirmation to the customer, title to the stock vests immediately in the customer.

In the instant case, the "purchasing broker", acting for its own account, failed to confirm the transaction, submitted a DK to the seller and disclaimed any interest in the securities. Can it be said that notwithstanding these facts, title vested in the Cross Claimants on November 1? We think not.

5. As part of the settlement, Satnick and Spingarn delivered releases, discharging Abraham of all claims in law or in equity "arising out of transactions in Westinghouse Electric Interim Securities on November 1, 1971". As the record owner of the Certificates on November 2, 1971, Abraham is entitled to a portion of the class action settlement. Such beneficial claims as Satnick and Spingarn might have had, arising out of the November 1 transaction, have been released.

CONCLUSION

It is respectfully submitted that Abraham sustained a loss with respect to the Interim Certificates that it held on November 1, 1971, and is a member of the class for whose benefit the class action settlement fund was created. It is further submitted that Abraham was the record and beneficial owner of the Interim Certificates on November 1, 1971 and remained their owner until February of 1973.

Respectfully submitted,

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Service of three ⓪ copies of the within
is admitted this 24th day of March 1977

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